

# **Private Sector Issues for the Ghana Poverty Reduction Strategy**

**September 2001**



**Sigma One Corporation**

**Private Sector Issues for the Ghana Poverty  
Reduction Strategy**

**Submitted to:**

**U.S. Agency for International Development  
Mission to Ghana**

**for:**

**Trade and Investment Reform Program (TIRP)  
Improved Policy Reform and Financial Intermediation  
USAID Contract Number: 641-C-00-98-00229**

**by:**

**Ralph L. Franklin  
Sigma One Corporation**

**In fulfillment of the following milestones:**

- 10.4 A brief on private sector issues to be incorporated into the poverty reduction strategy**

**September 2001**

**Sigma One Corporation**

## **Private Sector Issues for the Ghana Poverty Reduction Strategy<sup>1</sup>.**

---

This brief deals specifically with the role of the Private Sector as an engine of growth and a key element in the Ghana Poverty Reduction Strategy (GPRS). The GPRS is the product of a participatory process that involves: government, civil society organisations, the private sector and the donor community. This has culminated with a national level review and prioritisation at the National Economic Dialogue in May 2001. The broad goal of the GPRS is to provide a policy framework which will guide Ghana on a path of *equitable economic growth and accelerated poverty reduction within a sustained democracy*. The key elements of the Strategy have been identified as:

- Ensuring macro-economic stability for accelerated growth
- Increasing production and gainful employment opportunities
- Facilitating direct support for human resource development and the provision of basic services
- Expanding special programmes to support vulnerable groups
- Enhancing good governance

The private sector's principal role is in increasing production and creating gainful employment opportunities. The private sector can also play an important supporting and indirect role in the facilitation of human resource development and the provision of basic services. This brief, however, deals primarily with the private sector's direct role of expanding production and job creation.

The issues outlined in this brief focus on a tiered approach to private sector poverty alleviation based on the recommendations of the draft Ghana Poverty Reduction Strategy. This approach relies on markets and private initiative to: identify market requirements in local, regional and global markets; the production of goods and services that meet the quality standards demanded in those markets; and to expand into those markets through collaboration and investment. A framework for understanding how profitable activities and access to markets allow households to improve their incomes, is presented. The brief takes as given the implementation of the GPRS macroeconomic targets and objectives -these are necessary conditions for accelerated poverty reduction through private sector action. The framework is used to illustrate how appropriate macroeconomic policies can facilitate poverty reduction. The role of the private sector to finance (through compliance with tax and other rules regulations) the extension of public services to the poor is acknowledged. The actions specifically enumerated in the GPRS on production and gainful employment which are in keeping with this brief noted in the appendix.

---

<sup>1</sup> Prepared for the Republic of Ghana, Ministry of Economic Planning and Regional Integration and the Ghana Poverty Reduction Strategy Team, by Ralph Franklin, Senior Policy Analyst, Sigma One Corporation, in August 2001, under USAID's Trade and Investment Reform Program - Contract No. 641-C-00-98-00229.

## Macro Economic Instability Hurts the Poor

Macro-economic instability has been the principal cause of the high-cost, high-risk environment that has prevented Ghanaian firms from creating high paying jobs for the Ghanaian labour force. This nature of the Ghanaian economic environment reduces the returns to farming production and non-farm small enterprises as well. In fact, the damaging effects of economic instability have a higher incidence on the poor and on small scale enterprises, because they have few assets with which to avoid the high costs of doing business in Ghana.

The elements of the strategy that seek to ensure macro economic stability, as presented in the GPRS, are the necessary conditions for the private sector to assume its proper role in increasing production and creating gainful employment opportunities. Without effective implementation of the macroeconomic elements all the other elements cannot be fulfilled.

## Poverty in Ghana.

The GPRS seeks to respond to the problems of poverty in Ghana, which measured by substandard consumption levels and poor access to basic services, are large. Poverty is a persistent problem that is concentrated in the rural sectors of the country (**Table 1**). There are problems of poverty in urban areas but these reflect the translocation of the rural poor to urban areas. The depth of poverty is deepest in the three northern most regions of the country, while the prevalence of poverty is lowest in Accra. The diagnosis in the GPRS recognizes that while there has been progress in poverty reduction, the rate has been insufficient to lower the absolute number of persons living in conditions of poverty.

Region	Prevalence of Poverty
<b>Urban</b>	<b>19%</b>
Urban Coastal	24%
Urban Forest	18%
Urban Savannah	43%
Accra	4%
<b>Rural</b>	<b>49%</b>
Rural Coastal	45%
Rural Forest	38%
Rural Savannah	70%
<b>All Ghana</b>	<b>40%</b>
Derived from Table A1.2. "Poverty Trends in the 1990's", GSS, 2000.	

According to the diagnosis in the strategy document, public spending on health, education and sanitation is not well focussed on the poor. This is compounded by inappropriate timing and design of services. Management of direct poverty reduction activities is too removed from the intended beneficiaries.

In examining poverty in Ghana by the principal economic activity of households in Ghana (**Table 2**), food crop farming and export farming in the rural sector, non-farm self-employment and private informal sector workers (both urban and rural) exhibit the highest levels of measured poverty. These

households are poor because the value received for the goods and services produced and sold to the market is inadequate to acquire the “socially” desirable minimum pattern and volume of consumption. This situation includes the low value of the labour time sold to the market as wage workers or as informal sector entrepreneurs. The lower the value of time (services) and goods sold to the market, the fewer of these (goods and services) that are offered to the market for sale, until the household reverts into a pure subsistence household. Rural subsistence farming and urban informal activities are the result of low market valuations for goods and services supplied by the poor. These low market valuations for what the poor people can sell are the result of Ghana’s high-cost, high-risk economic environment.

### **A Market Based Framework for Poverty Reduction**

This brief is based on the market linkages, tenuous though they may be, between the resource allocation decisions (time, effort and production) of poor households with the economic environment that determines the market valuations of labour effort and goods sold by these poor households. This perspective is based T.W. Shultz’s Nobel Lecture “The Economics of Being Poor” (1979) and Michael Porter’s Competitiveness of Nations (1990). These perspectives provide a consistent framework for private sector initiatives for poverty reduction through a stable and competitive economy. Households and their members’ (women, men and children) interact with the markets in the following four ways:

- Sell the time of their members to the labour market (wage work or services)
- Sell goods and products
- Sell goods and services to itself for internal consumption
- Buy goods and services from other households and firms.

#### ***Profits are Essential***

In a competitive market economy, to which Ghana aspires, profits are the essence of private initiatives whether the firm is a large transnational or a simple street hawker. Profits (which are the excess of market price over cost) are needed to remunerate prior investments and entrepreneurial risk taking. These also serve as the basis for financing future growth regardless of how growth is ultimately financed, *e.g.* by borrowing, selling equity shares, or from internally generated cash. Profits are, therefore, the essence of sustainability for any private sector initiative in the GPRS.

#### **The importance of profits - even hawkers invest.**

The example of a simple street hawker is illustrative. A street hawker must invest to make her enterprise viable. She must invest in appropriate clothing and invest in the time and expense of reaching the most favourable vending site. The hawker must invest in meals to sustain herself during the period she is working as a hawker, and the hawker must invest the time on location.

Even hawkers need capital and credit relationships. The hawker needs the resources to either purchase the goods to be sold or needs to be credit worthy to the provider of the goods to be sold.

These investments need to be the most profitable opportunity available to her or she will dedicate herself to another activity - even if it means simply waiting for conditions to change by staying at home.

### ***Competitiveness of Firms***

Firms need to be profitable in order to survive and grow. In the context of poverty reduction, highly competitive firms can contribute to poverty reduction through generation of employment and higher remuneration to workers and entrepreneurs as productivity increases and firms produce consistent streams of profits. Firms can become highly competitive by improving the quality of their labour and material inputs. It is this process by which increased private sector competitiveness leads to increased creation of higher paying jobs within the private sector. This is true for all firms regardless of scale of employment.

From this perspective, high drop-out rates from primary and junior secondary schools are symptoms of low returns to schooling, because firms operate in a high-cost high-risk environment and cannot demand high quality skilled labour for their productive activities. In an alternative more competitive environment, highly competitive firms will pass “back” their demands for skills and skilled labour and create an impetus to improve schooling and improved incentives for school retention.

### **The Program of Macroeconomic Objectives and Outputs from the GPRS.**

The GPRS calls for specific actions in the policy fronts which are necessary for creating an environment in which the private sector expands production and creates better paying jobs. The program focuses on three areas of macroeconomic policy: fiscal policy, monetary management and international trade. The production and employment effects of these policies are illustrated in the following section.

### ***Fiscal Policy***

The improvements in fiscal discipline focus on three key actions: 1) improvements in the management of the public debt in order to reduce the interest burden on government and releasing fiscal resources for more productive uses; 2) improved public expenditure management to reduce the risks of unexpected surges in interest rates and inflation; and 3) specific proposals for improving fiscal resource mobilization to create a more neutral structure of economic incentives that will permit firms to improve the productivity of all their resources.

Resolving the problem of government debt “crowding out” private sector borrowing will improve access to production credit for farmers and all producers. Dealing with the government debt will improve access to longer term credit for capital and equipment investments. Exporting firms would increase their ability to meet international commitments. These effects together will increase employment and wages as profitable firms of all sizes are able to grow more rapidly.

Better debt management and lower interest rates will help reduce the de-capitalizing effects of high and volatile real interest rates allowing all producers (farmers, small and micro enterprises and export firms) to extend their investment horizons. These policies would facilitate adequate capitalisation of small and micro enterprises (SMEs) and promote their movement into the formal sector. In all production activities, firms would see an increased ability to modernize and expand. These benefits would be manifested on the worker's part in increased employment opportunities in enterprises with better inputs, equipment and higher productivity and wages. Improved management of the domestic debt and improved fiscal mobilization will reduce interest rates and will reduce firms' reliance on their internal cash flows to fund growth as greater participation in financial markets become possible.

Reviewing and revising existing taxes, fees, and user charges, to reduce the excessive reliance on trade taxes will promote outward oriented activities and investment by exporting firms in new markets and products. This will also create incentives for investment in technology and the use of inputs driven by expected returns. These changes in the regulatory environment will promote formalization of SMEs.

Better expenditure management on the part of government, particularly in managing its wage bill, will make rural activities more attractive. Small and micro enterprises would see wages become more closely tied to productivity. Exporting firms would begin to enjoy higher margins on their products. Workers would benefit from a wider range of employment opportunities, and be able to have more choice of employer. Wages in uncompetitive activities would fall but increases in employment demand would begin to deliver more employment opportunities at higher incomes as a result of broad-based growth.

### ***Monetary Management***

The monetary management policy actions will help facilitate private sector responsiveness and create employment growth opportunities. Reducing inflation and stabilizing the exchange rate will lead to lower nominal interest rates. This will reduce the risks and costs of doing business in Ghana. Competitive real interest rates are needed to enable firms to use productive factors optimally. Reducing the impact of foreign exchange flows on domestic monetary aggregates is needed to reduce costs arising in the economy wide incentives framework. Implementing the monetary management recommendations would extend the time horizon for users of credit and promote modernization and expansion in all profitable economic activities. The reduction in the banking system being "forced" to finance government will result in increasing use of financial institutions by farmers and producers and in increasing access to trade credit for exporters. These changes in turn will generate increased demand for labour of all types, skilled labour in particular, as firms are able to finance appropriate capital and input investments. Workers wages would rise with increased productivity and firm profitability.

The large spreads in interest rates are symptoms of riskiness in the Ghanaian economy. Increasing the transparency of the Bank of Ghana's operations will reduce the costs of doing business by lowering the risk premium required by investors in Ghana. The actions targeted at revising the laws and procedures which govern the banking sector will help reduce risk and lower the transactions costs in financial markets. This would increase access to investment for enterprises of all sizes.

The incentive to "dollarize" due to the inflation effects of poor monetary management hurts exporting and import competing firms, taxes micro enterprises severely and undermines the effectiveness of monetary management policies. Effectively managing monetary policy would have multiple positive effects for farmers and producers by reducing the uncertainties they face. Better prices (return to their effort) would result as farm gate prices would reflect world markets valuations. Exporting firms would be more competitive and credible in world markets. Market linkages between micro enterprises, established firms and buyers in local, regional and global markets would be enhanced, throwing off benefits (profits, knowledge, technology and skills) to all participants. The reduction in inflation and its variability would reduce the disproportionately high burden SMEs currently face. Value added activities would be stimulated as credit would expand and returns to market intermediation to domestic activities will improve. Workers would benefit from the increases in economic opportunities and would see reductions in the wage eroding effects of inflation. Workers would see the development of better opportunities for retirement saving as capital markets deepen.

### ***International Trade***

The macro economic actions to promote international trade are consistent with creating and promoting Ghanaian firms which must be competitive in all markets; they need to compete in regional and global markets to achieve optimal firm size and productivity. Improving export competitiveness through prudent exchange rate management (and stable macro economic policies) will help Ghanaian firms identify profitable export opportunities, reduce their domestic costs (through lower risk and lower costs) and make the best use of Ghanaian resources, primarily labour. Streamlining the import-export regime will lower transactions costs of exporting and importing complementary inputs. This will reduce the cost of international trade, costs that have a dis-proportionally higher impact on small and emerging firms.

Elimination of the dispersion in the tariff structure, reducing tariff exonerations and streamlining customs and inspections procedures will improve incentives for exports and would help exporting firms expand volume. Ghanaian firms would see productive activities as more attractive than simple intermediation (trading), and there would be reduced incentives to evade legal trade. Agriculture in particular would benefit from low and uniform tariffs and increased trade in agricultural inputs.

Agriculture and agricultural exports would receive better prices and higher incomes arising from increased opportunities in the farm to market value chain as a result of the improvements to the trade regime and the administration of trade.

### **Increased Production and Employment Through Private Sector Initiatives**

The GPRS recognizes that the government's creation of an enabling economic environment for improved private sector production will require that the private sector develop a more entrepreneurial approach. The GPRS notes that the "average food crop farmer has limited contact with the product market." As such, farmers are not likely to use many technological inputs. Improvement in the macro economic framework will clarify the opportunities for both farmers and input vendors. The GPRS notes weaknesses in the marketing and distribution network and recognizes that most farmers are not part of the currently limited marketing chain that exists in Ghana. Those who do find the costs to accessing the distribution channel very high.

The private sector strategy illustrated in **Table 3** focuses on actions that would begin to remove those constraints to accessing markets that hold Ghanaian household incomes down. The table summarizes the linkages between poor households and the market conditions that impinge on their income levels. As stated earlier, the principal causes of poverty in Ghana are low wages, underemployment for workers and low values and low productivity of the output from household-level enterprises. While the broad causes of these conditions are in the overall economic environment, poor households suffer from weak market linkages as a result. Table 3 presents a set of private sector actions that will serve to ameliorate poverty once the other elements of the GPRS are in place.

#### ***Low wages and under employment are the result of small markets.***

In particular, these actions include actions to access new markets, investments in improving product quality, increased competition in internal markets and extending the value chain linking international and domestic markets to domestic producers. To this end, the private sector must aggressively seek and serve new markets in ECOWAS, Africa and globally. In doing so firms must gain information about the goods and services these markets require and the quality and volumes needed to serve them. In order to meet these market demands, Ghanaian firms must cooperate to meet external market volume, timing and quality requirements. These same firms must also compete in domestic markets seeking input suppliers that meet their product needs.

The value to the household of a members' labour output is low in Ghana primarily because the skill level of workers for the most part is low. Paradoxically, there is a relative scarcity of workers with the job experience and training to meet the needs of emerging market opportunities. The lack of a deep

stock of skills in Ghana's labour force emphasises the need to generate rapid increases in employment and begin to create opportunities for workers to increase their skills levels through on-the-job training.

In summary, firms of all sizes face the relatively small internal market because they do not yet possess low enough cost structures and products of sufficient quality to access larger global and regional markets. The lack of access and knowledge of other markets is aggravated by the lack of access to technology and capital. Additionally they possess inadequate information of what outside consumers want to buy. All these impediments to competitiveness are the consequence of decades of instability and an inward-oriented economic policy framework. Ghana must develop the entrepreneurial capacity to find and serve new markets. As Ghanaian firms penetrate some of these new markets, firms will find that it is in their best interest to invest in skills formation of their workers. To help this learning process, for both the workers and the entrepreneurs, market opportunities must be sought in partnerships up and down the marketing chain.

Ghanaian firms must begin to compete with each other and collaborate when reaching outside Ghana's borders. This will be particularly important as export markets grow, because the ability to meet production orders in terms of volume and quality will become increasingly important. The need to collaborate in meeting these orders and on developing market information to penetrate and expand in foreign markets to increase profits and sustain growth. Effective trade associations can provide an excellent venue for increasing the competitiveness of firms in Ghana in this manner, allowing firms to share the burden of identifying new market opportunities and on how to access them. Trade associations can help share the burden of acquiring the knowledge required to enter new markets and help establish quality standards to protect the Nation's reputation in foreign markets.

***Low incomes are due to low productivity and high costs of serving markets***

The low value of household production is a consequence of the high costs faced by poor households in serving the markets they sell into. Transportation is expensive and often difficult; these producers lack the capital to acquire technology which could increase the value of their products and they are often unaware that the market demands different quality standards than they normally produce. They also suffer from poor connections to their suppliers and often have difficulty expanding production to meet market demand.

Private intermediaries are the agents that serve as the links in the value chain, connecting households and firms production to buyers, unnecessary restrictions on trade, high costs in the transporting products to market and poor access to market information limit the ability of these agents to play their part in transferring value between buyers and producers.

<b>Table 3. Market Oriented Approaches for Private Sector-Led Initiatives for Poverty Reduction in Ghana.</b>			
<b>Diagnosed Causes of Poverty in Ghana</b>	<b>Market Conditions Faced by Poor Households</b>		<b>Private Sector Initiatives for Growth in Income and Employment - Actions Required</b>
	<b>Household Supply Side Issues</b>	<b>Firm's Demand Side Issues</b>	
<b>Low Household Incomes:</b>			
<ul style="list-style-type: none"> <li>• Low wages and underemployment</li> </ul>	<p>Low level of Worker skills</p> <p>Low returns to Investments in Human Capital</p> <p>Few opportunities for acquiring job related experience (OJT).</p>	<p>Small markets for output of firms</p> <p>Firms are not located where poor people reside.</p> <p>Undercapitalized firms lack modern technology</p> <p>Firms are not competitive in terms of costs and quality (Domestic, Regional &amp; Global Markets).</p> <p>Low entrepreneurial capacity to find and serve new markets</p>	<p>Ghanaian firms aggressively seek and serve new markets in ECOWAS, Africa &amp; Globally.</p> <p>Ghanian firms invest in skill formation of their workers</p> <p>Ghanaian firms enter into "smart" partnerships with "upstream" and "downstream" suppliers/buyers.</p> <p>Ghanian firms cooperate and compete to promote high quality production to meet global standards.</p> <p>Business associations enhance entrepreneurial capacity of their members.</p>
<ul style="list-style-type: none"> <li>• Low Value for Products sold by Households</li> </ul>	<p>Costly logistics to serve markets</p> <p>Lack of technology to produce high-value products</p> <p>Lack entrepreneurial awareness of market demands for quality standards</p>	<p>Lack of Market information</p> <p>poor "downstream" market linkages for high value goods</p>	<p>Publicly funded market information disseminated widely and reliably</p> <p>Private sector local level marketing enterprises (Buyers) linked to higher level (value) markets Domestically, Regionally &amp; Globally.</p> <p>Private sector supplies high quality inputs for production.</p>
<ul style="list-style-type: none"> <li>• Low Productivity of Household Enterprises</li> </ul>	<p>Lack of inputs, skills and technology.</p>	<p>Poorly connected to markets</p>	<p>Improved market linkages through private intermediaries.</p>

**Specifically the following types of activities are recommended to promote private sector employment and poverty reduction:**

**Actions to Promote Larger Markets**

- Ghanaian firms must aggressively seek and serve new markets.
- Private firms, trade associations and government need to collaborate on developing market information and quality standards.

**Actions to Promote Product Quality**

- Ghanaian firms must invest in skill formation of their workers
- Ghanaian firms enter into “smart” partnerships with “upstream” and “downstream” suppliers and buyers.
- Ghanaian firms cooperate and compete to promote high quality production in order to meet global standards.

**Actions to Promote Product Volume.**

- Business associations must work to enhance entrepreneurial capacity of their members.
  - Private sector local level marketing enterprises (Buyers) need to be allowed to link to higher level (value) markets.
  - Private sector suppliers of high quality inputs are needed for improved production
  - Market linkages need to be enhanced through private intermediaries.
-

## **Specific Actions Recommended in the Draft Ghana Poverty Reduction Strategy Section on Production and Gainful Employment that are Consistent with Private Sector Led Poverty Reduction.**

---

The GPRS within the section on proposed actions for Production and Gainful Employment, the following proposals stand out as being consistent with private sector led initiatives:

### **In section 3.4.3.1: *Increasing Agricultural yields through Infrastructure, market and extension service provision.***

#### **Improving Market Access to Agricultural Producers**

- Point v.** Marketing and distribution systems to achieve competition improved.
- Point vii.** Market information is compiled and disseminated.

#### **Increased Access to Inputs and Services for Production**

- Point ii.** The seed industry that has been largely privatised, is supported and involves farmers in seed multiplication. The seed growers association scheme is expanded

### **In section 3.4.3.2: *Increasing Production and Employment by Promoting Agro-processing***

#### **Providing spatial and locational legality, facilities and services**

- Point ii.** Incentives to attract entrepreneurs into agriculture and agro-processing are defined and exported.

#### **Supporting the development/establishment of agro-processing industries**

- Point i.** State agro-processing firms divested and revamped.
- Point ii.** Local level entrepreneurs are supported.
- Point iv.** Proven rural entrepreneurs supported

### **In Section 3.4.3.4: *Improving Productivity in the Industrial and Service Sectors***

#### **Creating an effective institutional support structure**

- Point iv.** The provision of management training for small businesses is supported.
- Point vi.** An information base that assists firms with information on new technology, materials and production techniques is created.

### **In Section 3.4.3.5: *Increasing the Production and Exports of Non-Traditional Exports (NTEs) and NTE Development.***

#### **Making investments in trade support infrastructure**

- Point i.** Target feeder roads investments to export producing areas.
- Point ii.** Support the development of a cold chain to facilitate export of horticultural products.

**Supporting the development of private sector activities for exports of NTEs**

- Point i.** Generate sufficient volume and co-operation between exporters
- Point ii.** Develop new, mutually beneficial methods of contracting in out-growers schemes.
- Point iii.** Support capacity building for business and farm managers in export activities
- Point v.** Policies for cordial labour and industrial relations formulated and implemented

**In Section 3.4.3.6: *Increasing employment opportunities for poor communities***

**Formulating a Manpower Development Plan.**

- Point i.** National labour market statistics defined.
- Point ii.** Strategies for strengthening existing institutions to set standards and ensure quality training for apprentices.
- Point vi.** Labour laws reviewed to enhance industrial growth.
- Point vii.** National occupational safety and health policy for safe and healthy working environment implemented.
- Point ix.** Current and future manpower needs determined in collaboration with stakeholders such as training institutions and trade associations.